This record is a partial extract of the original cable. The full text of the original cable is not available.

UNCLAS SECTION 01 OF 02 LAGOS 001917

SIPDIS

SENSITIVE

DOE FOR DAS JBRODMAN AND CGAYE
TREASURY FOR ASEVERENS AND SRENANDER
USDOC FOR 3317/ITA/OA/KBURRESS

STATE PASS USAID FOR GWEYNAND AND SLAWAETZ
STATE PASS EX-IM FOR JRICHTER AND KVRANICH
STATE PASS OPIC FOR ZHAN AND JEDWARDS
STATE PASS TDA FOR NCABOT AND BTERNET

E.O. 12958: N/A
TAGS: EPET EINV NI ENERG
SUBJECT: NIGERIA ENTERS DEEPWATER ERA AS BONGA GOES ONSTREAM

Summary

¶1. (U) Nigeria entered the era of major league deepwater oil and gas production on November 28, as Shell Nigeria Exploration and Production Company (SNEPCO), announced its Bonga oil field began production. Bonga will initially produce 225,000 barrels per day (bpd) of crude oil, for a total of 1 billion barrels of oil over 10 years. It will raise Nigeria's daily oil output 10 percent from its current 2.4 million bpd. Bonga gas will be exported as liquefied natural gas (LNG) via the Nigerian LNG (NLNG) facility. However, reaching this point has not been problem free. The project has been plagued with cost overruns and scheduling difficulties that made project completion fall two years behind schedule. The National Assembly has launched an inquiry into the cost overruns.

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Bonga Begins Production, Ushers in Deepwater in Nigeria
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¶2. (U) On November 28, SNEPCO (Shell Nigeria's deepwater exploration and production company), announced Bonga oil field began production. SNEPCO management expects Bonga, the first major Nigerian deepwater field to go into production, to commence exports in January 2006. Bonga will initially produce 225,000bpd of crude oil, peaking at 350,000bpd, and producing about 1 billion barrels of oil over 10 years. Bonga will also produce 150 million standard cubic feet (mscf) of associated gas, and 280,000 bpd of fluids daily. Associated gas will be piped to Nigeria Liquefied Natural Gas (NLNG) for export to U.S. and European markets via a 268-kilometer Offshore Gas Gathering System. Bonga is located in oil mining lease block (OML) 118, about 150 kilometers from shore southwest of Warri, Delta State, at a depth of approximately 1000 meters.

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Bonga Key to GON Goals of Increased Oil Production
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¶3. (U) Cementing Shell's status as Nigeria's largest oil producer, Bonga will increase Shell's production in Nigeria by over 22% from its current 1 million-plus bpd output. At full production, Bonga will raise Nigeria's daily oil output 10 percent from its current 2.4 million bpd (barrels per day). The GON has targeted oil production of 4 million bpd of oil by 2010.

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Bonga Pioneers Super-FPSO Oil Production in Nigeria
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¶4. (U) The Bonga field produces via the Bonga Floating, Storage, Production and Offloading (FPSO) vessel, which taps into a network of 30 seabed wells. FPSOs are enormous tankers converted for deepwater oil and gas production, used in place of traditional fixed production platforms. With Bonga, Shell pioneers the use of "super-FPSOs" in Nigeria. Shell claims the Bonga FPSO, at 300,000 metric tons, is the world's largest such vessel.

Bonga Field a Joint Industry Effort

¶5. (U) The GON awarded the Bonga project to Shell during Nigeria's first deepwater bid round in 1993. It is operated by SNEPCO, on behalf of the national oil company, the Nigeria National Petroleum Corporation (NNPC). Under the Production Sharing Contract (PSC) model, SNEPCO has a 55 percent stake in the venture, while with Esso (20 percent), Nigerian Agip Exploration (12.5 percent) and Elf Petroleum

Nigeria (12.5 percent) have minority stakes under a Joint Operating Agreement.

Bonga Plagued with Cost Overruns, Scheduling Difficulties; National Assembly Launches Inquiry

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¶6. (SBU) Bonga has been plagued with cost overruns, and the project was completed two years behind schedule. Bonga's original budget was USD 2.7 billion, but SNEPCO officials say the final price tag is USD3.6 billion. However, other sources report cost overruns nearly double the original budget. Last week, the National Assembly launched an inquiry into the project. Assembly members are concerned the project's cost overruns will significantly delay GON's receipt of proceeds from the project; under the PSC model, Shell fully recoups its development costs before it has to pay taxes or split profits with the GON. Shell counters that the construction cost overruns will be balanced out by current high oil prices. Shell forecasts that oil recovery will be faster than anticipated, and thus the GON will not suffer economically because it will begin to realize profits within the expected time frame.

Comment

¶7. (SBU) Although a success, Bonga is alloyed with some difficulties. Industry watches tell us the cost overruns and late delivery have raised questions about deepwater projects in Nigeria. The GON and NNPC appear convinced that full cost-recovery provisions in PSC contracts provide industry with no incentive to control costs for deepwater projects. They argue industry "gold plates" its deepwater projects, since development costs are written off of the company's tax bill once oil production begins. Industry has a very different view. They argue the GON's local content provisions forced Shell to bring the Bonga FPSO into Nigeria for work more efficiently done elsewhere. With little infrastructure in place to do this work, costs ballooned while and schedules collapsed. While the project is finally finished and publicly everyone is smiling, the arduous process of bringing Bonga on-line has left the GON and industry alike with mud on their faces and with suspicions about the credibility of the other. Indications are that Bonga will be a production success. However, both sides will have to try harder to understand the position of the other if Nigeria hopes to approach its potential in deepwater production.